

BILL # HB 2286

TITLE: tax credit; charitable organizations

SPONSOR: Yarbrough

STATUS: As Introduced

PREPARED BY: Juan Beltran

FISCAL ANALYSIS

Description

The bill would eliminate the requirement for a taxpayer to establish a baseline year in order to qualify for the tax credit for cash contributions to charitable organizations that provide assistance to low income residents, chronically ill or physically disabled children. The bill would also replace the self-certification requirement of charities with one under which the Department of Revenue (DOR) would determine eligibility based on certain documents furnished by such organizations. The bill applies retroactively to tax year 2009.

Estimated Impact

Based on currently available data and a set of behavioral assumptions described below, it is estimated that HB 2286 would reduce individual income tax revenue by \$(5.0) million in FY 2010, \$(5.9) million in FY 2011, and \$(7.0) million in FY 2012.

The impact of the bill depends on behavioral responses of taxpayers to the proposed changes of the credit, which are difficult to predict with certainty. For this reason, the estimates should be interpreted with caution.

Analysis

According to data provided by DOR, the credit was claimed by 25,587 taxpayers in tax year 2005 and 29,202 taxpayers in tax year 2006, for a total of \$6.6 million and \$7.9 million credits used, respectively. The average credit was \$258 in tax year 2005 and \$272 in tax year 2006.

Based on a five-year average growth of 18.5% per year for this credit, it is assumed that the number of claimants will increase to 34,600 in tax year 2007, 41,000 in tax year 2008, 48,600 in tax year 2009, 57,600 in tax year 2010, 68,200 in tax year 2011, and 80,800 in tax year 2012. Assuming the average tax credit per claimant is \$270 in each of these tax years, it can be inferred that the cost of the credit under current law would be \$11.1 million (\$270 x 41,000) in FY 2009, \$13.1 million (\$270 x 48,600) in FY 2010, \$15.6 million (\$270 x 57,600) in FY 2011, and \$18.4 million (\$270 x 68,200) in FY 2012. These cost estimates represent the expected cost of the credit under current law and are, therefore, referred to as the “baseline estimates” in the remainder of this section.

This analysis assumes that the baseline estimates above will be affected by 2 behavioral responses to the bill, 1 of which will raise the cost of the credit and 1 that will lower it. Each of these behavioral responses is discussed below.

HB 2286 Will Make the Use of the Credit Easier than Previously

Based on information previously furnished by the Valley of the Sun United Way and other qualifying charitable organizations, it is believed that many taxpayers that were actually eligible for the credit in prior years did not claim it due to the complexity of the credit calculation. Since HB 2286 would simplify the credit calculation considerably, by removing the requirement to establish a baseline year and amount, it is reasonable to assume that a number of previously “discouraged” yet eligible credit claimants would actually use the credit under the new provision. In other words, the elimination of the baseline year requirement is assumed to induce eligible taxpayers to actually claim the credit.

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Based on historical data, 3.0% of Arizona taxpayers are expected to itemize their deductions and claim the charitable tax credit in FY 2010. This percentage reflects only those taxpayers that would be both eligible for the credit and not deterred by its current complexity. Since HB 2286 would eliminate the “deterrence factor” associated with the existing credit calculation, this analysis assumes the bill will result in an increase of the total number of “itemizing” credit claimants by 50%.

The assumption above means that the number of itemizing credit claimants would increase (relative to the baseline estimates) by 24,300 ($48,600 \times 50\%$) in tax year 2009, 28,800 ($57,600 \times 50\%$) in tax year 2010, 34,100 ($68,200 \times 50\%$) in tax year 2011, and 40,400 ($80,800 \times 50\%$) in tax year 2012. It is further assumed that the filing distribution and average claim for these new itemizing credit claimants will be the same as under the baseline estimates. Thus, the cost associated with the removal of the “deterrence factor” is estimated to be \$6.6 million ($24,300 \times \270) in FY 2010, \$7.8 million ($28,800 \times \270) in FY 2011, and \$9.2 million ($34,100 \times \270) in FY 2012.

New Certification Requirements Under HB 2286 Will Disqualify Some Charities from the Credit

This bill would require a qualifying charitable organization to provide written certification to DOR under penalty of perjury that must include:

1. Verification of the organization’s status under section 501 (c)(3) of the Internal Revenue Code or verification that the organization is a designated community action agency that receives federal Community Services Block Grant monies.
2. Financial data indicating the organization’s budget for the prior operating year and the amount spent on services to residents of the state that receive federal Temporary Assistance for Needy Families benefits, are low income residents, are chronically ill, or are physically disabled children.
3. A statement that the organization plans to continue spending at least 50% of its budget on services to residents of the state who meet the criteria described above.

Under current law, charities are not required to provide such documentation to DOR.

According to DOR, there are currently 805 self-certified charitable organizations in the state. It is expected that a number of these charities will not meet the more stringent certification requirements under HB 2286. To the extent that previous donors to such organizations do not reallocate their contributions to other qualifying charities, the claim of the credit will decrease.

Data from DOR indicates that more than 50% of donations for the purpose of this credit are consistently directed to a group of 12 well-established charities, such as the United Way, Habitat for Humanity, and the Salvation Army. Under the baseline estimates, this list of top 12 organizations will receive approximately \$6.9 million in FY 2010, \$8.2 million in FY 2011, and \$9.7 million in FY 2012. Other agencies, which are not identified, will receive the remaining donations of \$6.2 million in FY 2010, \$7.4 million in FY 2011, and \$8.7 million in FY 2012. For the purpose of this analysis, it is assumed that 25%, or approximately 198 of the smaller organizations will become ineligible under HB 2286. Under this assumption, the cost of the credit would decrease by \$(1.6) million ($\$6.2 \text{ million} \times 25\%$) in FY 2010, \$(1.9) million ($\$7.4 \text{ million} \times 25\%$) in FY 2011, and \$(2.2) million ($\$8.7 \text{ million} \times 25\%$) in FY 2012.

To conclude, it is estimated that HB 2286 would increase the net cost of the charitable tax credit by \$5.0 million in FY 2010, \$5.9 million in FY 2011, and \$7.0 million in FY 2012. The table below summarizes the estimated state General Fund cost (in millions of dollars) for each of the 3 behavioral responses included in this analysis.

Behavioral Responses to HB 2286	FY 2010	FY 2011	FY 2012
Greater Use Due to Less Complexity	6.6	7.8	9.2
Reduced Use Due to Certification Process	(1.6)	(1.9)	(2.2)
Net General Fund Cost	5.0	5.9	7.0

Local Government Impact

Each year, incorporated cities and towns receive 15% of income tax collections from 2 years prior. This bill would reduce local government distribution by \$(750,000) in FY 2012, \$(890,000) in FY 2013, and \$(1.1) million in FY 2014.